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## ABSTRACT

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The Cold War is over, the communist threat is gone and the global community has shifted from a bipolar to a multipolar world. Old alliances established as security against the threat are in question. The need for the United States to expend military resources abroad are not as clear cut as they once were. The American people focus inward on their standard of living, the economy, and overall well-being. The strains of trade deficits are tearing at the long established relationship between the United States and Japan.

This paper addresses economic relations, focusing on the causes of the economic imbalance between the United States and Japan since World War II. There are many sources available that identify, empirically, the extent of this economic imbalance. The paper outlines the causes that led to this imbalance and discusses the effects it has on the economic welfare of the United States and the future relationship with Japan. The paper focuses on the macro-level economic issues and does not consider the specific industries or commodities where imbalance occurs.

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*Define national security as the absence of acute threats to a minimally acceptable level of basic values deemed essential by society. If material well-being is considered to be a societal value, it follows from this definition that any event that interferes with the flow of trade and so reduces a trading nation's economic welfare constitutes a threat to its national security.<sup>1</sup>*

## INTRODUCTION

In the realm of academics, national security policy focuses on five elements--foreign policy, defense policy, international economic policy, intelligence policy, and domestic policy.<sup>2</sup> This paper addresses United States - Japan economic relations, focusing on the causes of the economic trade imbalance between the United States and Japan since World War II. The purpose is not to validate whether an imbalance or bilateral trade deficit exists, that is a fact. There are many sources available that identify, empirically, the extent of this trade imbalance. This paper outlines causes that led to this imbalance; discusses the effects of the imbalance on the economic welfare of the United States and its relevance to United States national security; and posits alternatives for dealing with it. The paper focuses on macro-level economic issues and does not consider the specific industries or commodities where imbalance occurs. But, before we proceed we need to answer the question of, "Why is trade or economic policy of such importance?" The answer, as identified by Stephen Krasner (1987), lies in three areas. First, trade policies may be used by nations to promote its power in the world community relative to other nations. Second, one nation may want to effect another's military, social, or political actions. In this case, trade policies

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<sup>1</sup> Jim Leitzel, Economics and National Security, (Colorado: Westview Press, 1993), p. 91.

<sup>2</sup> Russell L. Gilbert, The U.S. - Japan Security Alliance: Will it Survive in the New World Order?, (Pennsylvania: U.S. Army War College, 1991), p. 82.

may be developed which force trading partners to react in a more preferred manner. Third, overlooking the short-term economic costs of trade policies, nations may forge trade policies that will better achieve long-term political and security objectives.<sup>3</sup>

Economic issues have now risen to the level of importance of security and political issues.<sup>4</sup> From a national perspective, bilateral trade deficits should not matter. In today's world, bilateral deficits with one nation can be offset by surpluses with others. At the macro-level, however, trade deficits do matter because they usually require borrowing from abroad or using holdings of exchange reserves or precious metals to finance them. The bilateral deficit with Japan has become a policy concern because it is a greater share of the total deficit and continues to grow. The bilateral deficit also reflects underlying competitive struggles between traditional United States firms and Japanese competitors. As America's economic superiority continues to decline, political relations will continue to worsen. In 1991, Americans rated Japan as the biggest threat to the United States. With such problems as massive debt, trade deficits, a faltering health service, a defunct education system, and crime-ridden and violent cities, it is unlikely that American citizens will be willing to support overseas military commitments. This is especially true when faced with the reality that Japan is an economic rival. "From a macroeconomics perspective, while most trade policies do not effect the overall level of United States trade deficit, they can affect its composition. For individual United States industries, composition is everything. It reflects how

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<sup>3</sup> Leitzel, p. 95.

<sup>4</sup> Winston Lord, "U.S.-Japan Policy and the New Japanese Government, Joint Hearing Before the Subcommittees on Economic Policy, Trade, and Environment and the Asia and the Pacific of the Committee on Foreign Affairs House of Representatives, (Washington, D.C.: U.S. Government Printing Office, 1993), p. 13.

well they are competing and whether they are expanding and generating profits or shrinking and incurring losses."<sup>5</sup>

The chairman of Daiwa Securities, Yoshitoki Chino, believes that Japan's competitive edge results from two simple ideas. One, the Japanese are self-reliant and devoted to hard work. Two, they do not wage war. He believes, by not destroying the nation's economy in war, reserving resources for more productive ends than on building armaments, a hardworking nation will become more prosperous.<sup>6</sup> The Japanese have been particularly astute at taking advantage of adapting and pulling together culturally and nationalistically. The Japanese economic 'miracle' can be said to be built upon this strength. This strength has resulted in first, allowing the Japanese to do better what the United States has been doing for years. The Japanese imported their language and culture from China and Korea; today they import business and technological knowledge. Second, the Japanese culture is such that they are willing to sacrifice a great deal personally in order to achieve national economic goals. Third, Japan has the patience to integrate the requirements of the free market into the larger and longer-term needs of its society. This requires national planning and cooperative consensus, something the United States has not done so well.<sup>7</sup>

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<sup>5</sup> Dick K. Nanto, "Congress and Trade Policy Toward Japan", CRS Report For Congress, (Washington: United States Congress, 1992), p. 4-5.

<sup>6</sup> Daniel Burstein, YEN! Japan's New Financial Empire and Its Threat To America, (New York: Fawcett Columbine, 1990), p. 101.

<sup>7</sup> Burstein, p. 104-6.

## BUILDING JAPAN'S ECONOMIC FOUNDATION

United States emphasis on post World War II security concentrated on the Soviet Union's influence in Eastern Europe, North Korea, and China. The fear of the Soviets as a global threat to the United States prompted a firm alliance with Japan. In order to build upon this alliance, Japan's economic recovery following World War II became paramount. To aid in its recovery, United States policy objectives were:

1. To preserve the territorial and political integrity of Japan against Communist expansion or subversion;
2. To ally Japan closely to the United States;
3. To ensure political stability; and,
4. To support a prosperous, strong, and self-supporting Japanese economy.<sup>8</sup>

Recovery of Japan's economy was most important for three reasons. First, economic stability in Japan would prevent the social chaos that would make Japan vulnerable to Communism. Second, a primary interest of the United States was to make certain that Japan could no longer make war. Third, the "containment" of the Soviets and the spread of communism became the dominating factor in all United States foreign policy.<sup>9</sup> However, even beyond the cold war and balance of power, American goals of a multilateral economic system with large foreign markets for American exports required the revival of Japanese industry and trade. United States strategic and economic goals were mutually reinforcing. Therefore, by 1949 the United States had instituted a Japanese recovery program similar to the European Recovery Program (known as the Marshall Plan). The alliance was intended to guarantee the "balance of power" and a favorable

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<sup>8</sup> Roger Buckley, U.S.-Japan Alliance Diplomacy, 1945-1950, (Cambridge: Cambridge University Press, 1992), p. 5.

<sup>9</sup> George Friedman and Meredith Lebard, The Coming War With Japan, (New York: St. Martins Press, 1991), p. 106.

global economic climate for American producers. The latent productivity of Japan could readily be converted into military power as well. The United States sought at all costs to preserve its superiority over the Soviet bloc by retaining the loyalty of its defeated enemy. Balance-of-power considerations were paramount; the loss of Japan to the Soviets would irrevocably tip the balance in the Soviet favor.<sup>10</sup>

Much of Japan's industries were destroyed during World War II. However, less than one percent of its wartime business leaders were purged from their prewar posts. The very *zaibatsus* blamed for the rise of the Japanese militarism resurfaced after the war as conglomerate groupings known today as *keiretsus*. Today, Japanese companies are unlikely to break up these long-term corporate relationships that have been the traditional practice in Japan.<sup>11</sup>

To assure a strong alliance with Japan during the ensuing Cold War the United States set in motion the following policies. First, the United States did not dismantle the Japanese industrial bureaucracy. Second, the United States gave Japan free access to United States markets virtually with no conditions of in-kind treatment. Third, Article IX of the Japanese constitution did not allow Japan the use of military force except in protection of the home islands. By these moves and subsequent security treaties, however, the United States assumed full responsibility for the protection of Japan and maintenance of the peace in the Pacific.<sup>12</sup> The United States did not foresee the impact this would have on future United States economic stability. In 1950, when the Korean War began, Japan's economy had not developed to the extent hoped for by the United States. Therefore, at the outset of the war, the strategy implemented by the United States was for

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<sup>10</sup> William S. Borden, The Pacific Alliance, United States Foreign Policy and Japanese Trade Recover, 1947-1955, (Wisconsin: The University of Wisconsin Press, 1984), p. 11.

<sup>11</sup> Arthur J. Alexander and Hong W. Tan, Barriers to U.S. Service Trade in Japan, (California: The Rand Corporation, 1984), p. 39.

<sup>12</sup> Patrick Marshall, "The U.S. and Japan", CQ Researcher, (May 31, 1991), p. 331.

Japan to supply the United States with the production capacity needed to sustain this war. It was this strategy that was the catalyst to stimulating the economic recovery of Japan. Because of Japan's geographical location and the heavy strain on American industry by rearmament orders Japan was the most logical choice of supply for Korea. Even more critical for Japan, this strategy would furnish needed dollar-earning markets for Japanese industry.<sup>13</sup>

During this period, Japan erected tariff and quota barriers to imports. Under the 1949 Foreign Exchange and Foreign Trade Control Law, all imports required import licenses. The Ministry of International Trade and Industry (MITI) exercised a great deal of power through its control over granting import licenses. This, in effect, established quotas on all imports.<sup>14</sup> Japan, also, chose to make itself one of the most difficult nations for outside capital investment, forcing foreign companies into joint ventures, subjecting them to a wide range of controls, and prohibiting them from sending the profits back to the United States. Instead of relying on foreign capital, planners of postwar Japan adopted measures that forced Japan to generate its own capital surplus through savings and trade. Japanese industry used that surplus as it moved up the ladder of skill and technology toward competition with the world's industrial leaders.<sup>15</sup> Japan's domestic and international economic resilience can be attributed to Japan's continual sustainment of a complementary mix of official economic policies, corporate strategies, and innovations in production technology that are aimed at maximizing the size and strength of its industrial sector. When combined with already existing cultural and social values, such as group loyalty and devotion to work, a willingness to make short-term sacrifices to achieve long-term goals, and

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<sup>13</sup> Borden, p. 145.

<sup>14</sup> Edward J. Lincoln, Japan's Unequal Trade, (Washington: The Brookings Institution, 1990), p. 13.

<sup>15</sup> Burstein, p. 112.

perhaps most importantly, a collective desire to regulate the nature and extent of incoming foreign influence on the Japanese society, the result is a tremendous domestic and international organization.<sup>16</sup>

In 1960, the Treaty of Mutual Cooperation and Security replaced the U.S.-Japanese Security Treaty. One of the major provisions of this treaty focused on the economic relationship between the two nations. Article II of the treaty provides that, the United States and Japan will contribute toward the further development of peaceful and friendly international relations between them by strengthening their free institutions, by bringing about a better understanding of the principles upon which the institutions are founded, and by promoting conditions of mutual stability and well-being. The United States and Japan will also seek to eliminate conflict in their international economic policies and will encourage economic collaboration between each country.

Initially, the continued vigilance against the Soviet threat of communism led the United States to accept bilateral trade surpluses by Japan in order to maintain the security relationship.<sup>17</sup> The growth in Japan's economy between 1950 and 1990 represents the most rapid peacetime shift in relative economic status in the history of the world. Such explosive change on the part of a single nation could not but cause substantial apprehension to other nations. Helping fuel the resentment at the necessity to adjust is, of course, the fact that Japanese success is due in part to unfair trade practices, in particular the protection of Japan's local market from imports and the promotion of certain sectors for export-led growth. The argument on behalf of demanding reciprocity in access between the United States and Japan extends beyond mere Japan-bashing; the contention is that

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<sup>16</sup> Stephen Cohen, "U.S.—Japan Interdependencies", Hearings Before The Joint Economic Committee Congress of the United States, (Washington, D.C.: U.S. Government Printing Office, 1992), p. 4.

<sup>17</sup> Marshall, p. 332.

only a "results-oriented" approach will reduce the trade imbalance with a partner for whom the abstract appeal to "open-markets" has no meaning.<sup>18</sup>

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<sup>18</sup> Theodore H. Moran, "International Economics and National Security", Foreign Policy, (Winter 1990), p. 77.

## SAVINGS VERSUS CONSUMPTION

A fundamental cause of the imbalance between the United States and Japan is the fact that the savings and consumption in the two countries are so different. The United States consumes more than it produces and does not save enough to build the additional productive capacity to make up the difference, leading to a trade deficit that supplies excess American consumption and in flow of foreign capital that make up for the lack of American savings. Overall the savings and consumption imbalance in the United States are a much greater drag on American competitiveness, than trade barriers.<sup>19</sup> Japan's Confucian cultural tendency toward saving provided a good foundation for Japan economic designers to create pro-saving policy structures. Prior to World War II, the United States and Japan savings' rates were on par with each other, however, after the war, Japanese policies were specifically designed to promote savings. In contrast, America's postwar policies were consciously designed to promote consumption at the expense of savings. Today, Japan's 30 percent gross national savings rate, is about three times as large as America's. In the United States, the Internal Revenue Service penalizes Americans who save by taxing the interest they earn. In Japan individual savings' accounts have been allowed to accumulate largely untaxed.<sup>20</sup>

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<sup>19</sup> Moran, p. 78-9.

<sup>20</sup> Burstein, p. 115.

## MONOPOLIES AND REGULATIONS

General government regulations lay behind most of Japan's impediments to trade with the United States. The industry monopolies and cartels are creatures of government control and regulations. Even government purchases are tightly controlled—the government controls or influences the size and growth of the procurement market, the products to be procured, the specifications, terms and conditions, the timing, the winning vendor and follow-on procurement. When government itself is not the regulatory agency, the law gives authority to nongovernmental organizations (e.g., the bar associations) to regulate industries, with the sanctions of government in the background.<sup>21</sup>

Japanese government policies also have often emphasized benefits to industry over consumers, and have been prone to intervene in markets more than the United States government. The relationship between industry and government in Japan is much different from in the United States. In Japan, for example, the director of Nippon Electric Company phones Japanese officials three or four times a week. Whereas, in the United States the head of Bell Laboratories rarely calls the Commerce Department, if at all.<sup>22</sup>

Japan also has old laws still in effect that were created to provide protection while rebuilding her economy but are now outdated with today's global economy.<sup>23</sup> However, in the face of vigorous Japanese competition, the United States too has often turned a blind eye to its own policies and sought protection for its firms and workers. In industry after industry, from textiles

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<sup>21</sup> Alexander, p. 4.

<sup>22</sup> Clyde V. Prestowitz, Jr., Trading Places: How We Allowed Japan to Take the Lead, (New York: Basic Books, Inc., 1988), p. 16.

<sup>23</sup> Joseph S. Nye, Jr., "Coping With Japan", Foreign Policy, (Winter 1992-93), p. 96.

and steel, color television sets and automobiles to machine tools and semiconductors, American trade officials have successfully pressured Japan to restrain its exports to the American market. This has been done so often during the past 20 years that over 40 percent of Japanese exports to the United States are restrained by one or another arrangement.<sup>24</sup> In the United States, short-term profits versus long-term investment have become the American way. The Japanese have preferred long-term investment over short-term profits. Building long-term market share has been Japan's driving force. The major shareholders in most Japanese companies are other related companies. Investments by them are made in terms of the long-term strategic survival of the group. The necessary capital is relatively inexpensive, and the risk of investment is reduced by the nature of the group structure.<sup>25</sup> To put it in simpler terms: American investors demand short-term profit, while Japanese investors demand growth. Japanese corporations do not place the interests of their shareholders on the same level of importance as do American corporations. At times, financial institutions that lend money, suppliers of raw materials, distributors of their products, employees and various other related groups are considered to be of equal importance.<sup>26</sup> Another problem, obvious to some, facing American companies today, and one that has unknown costs is one of poorer quality. The same situation occurs when one looks at the productivity of the American labor force. One needs only to peruse the local book store and pickup books by such authors as Deming, Peters, and Juran to discover numerous accounts of quality and productivity

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<sup>24</sup> Gary R. Saxonhouse, prepared statement, "U.S.—Japan Interdependencies", Hearings Before The Joint Economic Committee Congress of the United States, (Washington, D.C.: U.S. Government Printing Office, 1992) p. 55.

<sup>25</sup> Prestowitz, p. 209.

<sup>26</sup> Kichiro Hayashi, The U.S.—Japanese Economic Relationship: Can It Be Improved?, (New York: New York University Press, 1989), p. 20.

problems that exist throughout the United States. Although quality and productivity advances have been made, these were severe problems for American businesses for more than a decade.

It can be said then, that three separate but interrelated problems comprise the heart of the United States-Japanese competitiveness problem. First, there are inadequate macroeconomic policies in the United States to promote more savings, higher productivity increases, and more capital formation. Second, adequate efforts by the American industrial sector to lower production costs, improve quality, introduce new products, and provide after-sales service to the extent necessary to successfully compete head-to-head with Japanese competitors in the United States and foreign markets have not been made. Three, a Japanese market, except for imports of high-value added manufactured goods, is still not as open or accessible as markets in other industrial countries.<sup>27</sup>

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<sup>27</sup> Cohen, p. 5.

## DEALING WITH THE PROBLEM TODAY

While the economies between Japan and the United States are becoming increasingly interdependent, it does not necessarily mean that it is favored, fixed, or proportionately advantageous to both. Stephen Cohen, in his comments before the Joint Economic Committee of the 102nd Congress of the United States, outlined four areas of interdependence between the United States and Japan. First, he implied that, in the largest sense of the international political and economic context, Japan is more dependent on the United States than the United States is on Japan. Japan has had only the United States as a close political friend and military ally since the end of World War II. Japan's foreign policy has revolved around maintaining American friendship, giving in to one United States economic demand after another rather than risking straining its strongest and most important legitimizing link with the outside world. The slightest hint of a shift to protectionist trade policies in Washington can cause panic in all of Japan's financial markets. Japan's industries need United States markets more than American industries need theirs. For all the talk of rising industrial strength, Japan as a whole is still not prepared to function independently of the United States in global political and economic affairs. It is this constant "giving in" on the demands of the United States that is straining Japanese support for a continued relationship with the United States. Second, in terms of pure economic theory, asymmetry and bilateral interdependence also favors the United States. Economists believe that the real wealth of nations comes from importing goods, not from exporting. Japan's trading policy, however, is still firmly rooted in the mercantilistic tradition of wrongly equating the maximization of trade surplus in manufacturing goods with maximization of national welfare. Japan exports substantial amounts of real economic resources in exchange for American paper

money. A large percentage of the dollars earned by Japan's trade surplus are then reinvested back into the United States, effectively subsidizing the American inclination for spending more than it can collectively produce as a country. When this is added to Japan's contribution to military burden sharing, the Japanese can be said to have assumed the role of chief foreign underwriter of American economic prosperity and overseas military power. Thirdly, the United States is ahead of Japan in cultural influence. When measured in terms of motion pictures, books, music, fast foods, sports, and overall lifestyles, the United States has an overwhelming surplus. The downside to this though, is that the income and royalties from sales are meager in comparison to the delusions they generate among most Americans. However, when measured in terms of real world ability of industrial sectors to compete, Cohen sees Japan decidedly ahead of the United States. This fourth and most important interdependence is one that will most heavily determine a country's increases in its domestic living standards and in its levels of influence and power on the international scene. The battle for the all-important high-technology sector between the world's two strongest, most talented, and most dynamic economies is arguably the most important contest in international relations for the 1990's and beyond. The economic costs of coming in second are enormous.<sup>28</sup>

United States trade policy toward Japan continues to rely on a few basic practices. One is the use of existing trade policies to address the problems of dumping and unfair trade practices. In times of rising yen value, antidumping laws become powerful weapons, since production costs in Japan go up with the appreciation of the yen. To the Japanese exporter this means he must raise prices of goods, cut costs, or risk antidumping consequences. Another practice has been for the Administration to request the Japanese government to levy voluntary export restraints (VER)

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<sup>28</sup> Cohen, p. 3.

in certain key industries. This has usually been done on behalf of major United States industries when new legislation or enormous antidumping penalties seemed unavoidable. This alternative has its appeal because VERs are temporary, do not necessarily incite retaliation, and do not appear as protectionist. Lastly, rather than closing United States markets to Japanese exports, the practice of increasing United States exports to Japan can be used. United States producers and Japanese consumers gain by reduced trade barriers in Japan. American companies can learn to do business in the Japanese market, increase production, create more jobs, and become stronger international competitors. Access to Japan's markets also appeals to the American sense of "fair-play". While Japan continues to maintain barriers to imports, the United States has focused its attention on barriers within Japan's domestic market. These are being addressed through the General Agreement on Tariffs and Trade (GATT), bilateral negotiations, and the Asia-Pacific Economic Cooperation.<sup>29</sup>

Other challenges may be more central to the United States-Japan relationship. In contrast to other industrialized nations, Japan imports little of the types of goods that it exports. As a percentage of GDP, Japan imports a disproportionately small share of manufactured goods, only about 3 percent of GDP and falling. The United States imports about 6.5 percent of its GDP in manufactured goods. For Europe it is 7.4 percent. We know that trade follows investment, and if investment is curtailed or restricted trade will not follow. Looking at the global stock of inward direct investment, about 38.5 percent of that global stock is in Europe and 28 percent is in the United States. Japan's disparaging investment is only 0.7 percent. This is a cause for concern.<sup>30</sup>

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<sup>29</sup> Nanto, p. 11. and USAF Air War College, Regional Security Analysis-Pacific Rim, Lectures, (December 1994).

<sup>30</sup> Charlene Barshefsky, "U.S.-Japan Policy and the New Japanese Government, Joint Hearing Before the Subcommittees on Economic Policy, Trade, and Environment and the Asia and the

## SECURITY IMPLICATIONS

The level of mutual bad feelings between the United States and Japan in the economic relationship is already quite high and has threatened to poison the security relationship. By altering the international flow of goods and services, a country's trade policy affects its economic relationship with the rest of the world. Trade policies affect the size of the gains from trade as well as the distribution of gains among trading partners. In distributing the existing degree of interdependence among nations, trade policy may well have an effect on a trading nation's security.

Trade policy is designed to shape its external environment by changing the behavior of other nation-states and nonstate actors, both domestic and foreign. By altering the economic gains through the trading relationship, a nation can influence changes in the actions of its trading partners. That is, trade policy can be incorporated as a tool of foreign policy.<sup>31</sup> With this in mind, two approaches to solving this dilemma have been proffered in overcoming these differences. The first approach is for America to start acting more like Japan—straighten up and fly right. That is, to concentrate on reestablishing its economic competitiveness by taking steps to decrease its federal budget deficit, provide incentives for increasing its savings rate, improving its educational system, directing more money into research and development, and continue to improve worker's productivity. This is easier said than done, however, for there are political constraints in the United States which prevent rapid or dramatic progress in achieving such changes. So, while progress moves at a snail's pace, Japan's trade surpluses with the United States continue to

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Pacific Committee on Foreign Affairs House of Representatives, (Washington, D.C.: U.S. Government Printing Office, 1993), p. 12.

accumulate. A second approach is to encourage Japan to be more like the United States. That is, to promote the Japanese consumer's demand for American goods while, at the same time, reducing the rate of Japanese savings which provides the means of cheap credit, to increase purchases of American goods and services by the Japanese government, and generally to endow individuals with the expectation of increasing standards of living goals rather than pursue economic competition so resolutely. This was the logic behind the Structural Impediments Initiative, which attempted to go beyond trade talks and actually change Japanese social behavior in ways that would be helpful to American business. Underscoring the Structural Impediments Initiative, and therefore most of American policy toward Japan, was the expectation that Japan and the United States were coming together socially as the Japanese economy modernized and became more intertwined with the United States. It was thought, by many, that the friction brought on by the Japanese trade surplus was temporary and would disappear in time as Japanese economic conduct began to be more like that of the United States. To the degree that American policymakers were dismayed of undertaking structural reforms to make the United States "more like Japan," this assumption of ultimate "coming together" became less a hope than a fundamental need for the long-term health of the relationship.<sup>32</sup>

As long as the bilateral treaty with the United States remains in force and United States troops stay in Japan, Japanese businessmen downplay the importance of Japan's military preparedness. It is this group that most strongly favors Japanese burden-sharing to maintain American forces in Japan. The alliance is seen by them, quite simply, as good for Japanese business. Japanese businessmen concern themselves about United States domestic economic

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<sup>31</sup> Leitzel, p. 95.

<sup>32</sup> Francis Fukuyama and Kongdan Oh, "The U.S.-Japan Security Relationship After the Cold War", (California: RAND National Defense Research Institute, 1993), p. 36.

controversy over the "unfairness" of Japanese trading practices. To keep the alliance intact, they have been willing to continually make economic compromises by opening markets, or in the new catch phrase coined by KEIDANREN, they desire *kyosei* [symbiosis] with the United States. They are unwilling, however, to succumb to unlimited pressure to alter the Japanese way of doing business.<sup>33</sup>

On the other hand, many Japanese believe that Japan can serve as a unique non-Western model of socioeconomic development germane to the rest of the Asian region or the world. This belief has drawn empathetic reaction from other countries in the region. The appeal of the Japanese model may be the force behind adjustments in Japanese foreign policy. This emphasis on Japan's economic model has mushroomed into a criticism of Western society as a whole, and more specifically American society. The Japanese think that American's are plagued by excessive individualistic attitudes and accentuate the rights of the individual or interest groups that place their own interests above those of the whole nation. These factors might infer that Japan and the United States are no longer automatically coming together, making it more difficult to maintain a strong security relationship.<sup>34</sup>

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<sup>33</sup> Fukuyama, p. 26.

<sup>34</sup> Fukuyama, p. 39-40.

## EFFECTS OF IMBALANCE

Until recently, the predominant political party in Japan, the Liberal Democratic Party (LDP), had been in power since its creation in 1955. The stability of the political system in the country brought about by being led year after year by the same party developed strong alliances with other centers of power in Japanese society. This enabled the LDP to push its economic policies and maintain continuity for the long term without being subject to change after each election as is done in the United States.<sup>35</sup> As the United States strives for decreasing the trade surplus with Japan, the majority of the Japanese fear that a significant drop in the nation's trade deficit would be detrimental for their domestic economy. This internal concern causes some Japanese bureaucrats to delay reforms that would open Japan's markets to American imports.<sup>36</sup> The United States and Japan will continue to disagree on economic issues, however, both will benefit in the long term from overall economic interdependence, especially if disagreements are constrained by a broader longer term strategic vision.<sup>37</sup>

Robert Gilpin, a Princeton political economist, believes that the world stability cannot rest much longer on Japanese-financed American hegemony. If the U.S.-Japan relationship collapses, the possibilities of a stable international political order may vanish as well. George Packard, the dean of the John Hopkins School of Advanced International Studies, predicts that if current policies do not change, the U.S.-Japan relationship will descend into protectionism, retaliation, recrimination, and a search for different partnerships. Japan would then link its destiny to the

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<sup>35</sup> Fukuyama, p. 25.

<sup>36</sup> Barry Hillenbrand, "America in the Mind of Japan", Time, (February 10, 1992), p. 23.

<sup>37</sup> Nye, p. 114.

Chinese or Soviets, seek to expand its growing economic influence in Asia and the Pacific, and end up in direct opposition with the United States.<sup>38</sup>

The economic welfare of one country depends on the events that take place in the other. When dependency between two national economies is mutual, a condition of international interdependence exists.<sup>39</sup> As suggested by David Baldwin (1980), this interdependence falls into two categories: sensitivity or vulnerability interdependence. "Sensitivity interdependence merely implies contingency. While, a vulnerable interdependence between two nations suggests that a breakdown of the relationship would be costly to either or both nations; that is there are opportunity costs of shunning the relationship."<sup>40</sup>

The interdependence of the United States-Japan relationship is likely to continue to be a source of bilateral friction between the two countries. The imbalance has not generated an affective American response. In stead, it has engendered a nonstop torrent of irrelevant rationalizations about the consequences of Japan's rising economic strength; oversimplified explanations as to its causes; exaggerated and irrelevant proposals to retaliate against Japan; and erroneous assumptions as to why the bubble of the Japanese economic miracle burst. A policy of attitudinal and management mismatch perpetuates a competitive asymmetry that is making the United States increasingly dependent on Japanese companies for the important products and technologies of the future, as well as on Japanese investors for capital inflows to finance a perennial current account deficit in United States balance of payments.<sup>41</sup>

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<sup>38</sup> Burstein, p. 21-2.

<sup>39</sup> Leitzel, p. 90.

<sup>40</sup> Leitzel, p. 90.

<sup>41</sup> Cohen, p. 4.

However, these interdependencies are not just between the United States and Japan. The sizes of the economies of these two nations have a tendency to have global effects. Any changes in balance, access, mercantilist or protectionist tendencies, isolationism, etc. will cause ripple affects throughout the world. Multilateral means must be used to solve conflicts for which nations have difficulty in finding a solution.

## U.S. MILITARY PRESENCE

United States military presence in Japan will continue to be critical for the United States as well as Japan. It will serve as the bedrock for security, open markets, and democracy in the Asia-Pacific region.<sup>42</sup> The threat of regional conflicts and decline of the bipolar world enhance the need for strong alliance with Japan. One of the ironies of the post-Cold War period is that globally there is more of a desire for America overseas military presence than before. With the unification of Germany, with the growing economic power of Japan, neither the Europeans nor the Asians, as a whole would welcome wholesale withdrawal of American troops. As United States economic power and influence continue to decay in Asia, the one bit of leverage that the United States does have is its military presence. However, the internal conflicts within the United States regarding the bilateral trade deficit will cause certain interests to call for isolationist attitudes, which others view as detrimental to the stability of the United States economy.

Japan's outstanding economic success can be attributed, in part, to the security guarantees that the United States has provided and the fact that the Japanese spend such a relatively small share of their GNP on defense.<sup>43</sup> A hard-line stance with Japan may fuel resentment without producing the desired result. With the combination of growing Japanese anti-Americanism and the evolving geopolitical environment it is plausible that the United States might push Japan too far and sever the US-Japanese alliance. The US-Japan relationship is a model for success, where an enemy has become a close and prosperous ally, tied intimately to United States diplomacy and

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<sup>42</sup> United States, A National Security Strategy of Engagement and Enlargement, (The White House, July 1994), p. 23.

<sup>43</sup> Representative Hamilton and Stephen Cohen (See discussion between them), "U.S.—Japan Interdependencies", Hearings Before The Joint Economic Committee Congress of the United States, (Washington, D.C.: U.S. Government Printing Office, 1992), p.27.

just as importantly its economy.<sup>44</sup> A fractured alliance could force Japan to align herself with Russia or China, either alliance would not be favorable for the United States. Japan must look inward at its business culture to determine whether it is engaging in voracious mercantilist practices. Rampant Japanese economic success in the face of dramatic economic decline in other nations does not bode well. After this inward look, if the Japanese are still satisfied that their economic practices are justifiable, then they should persuade other nations to adopt those practices as their own.<sup>45</sup>

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<sup>44</sup> Lance Marrow, "Japan in the Mind of America", Time, (February 10, 1992), p. 18.

<sup>45</sup> Fukuyama, p. 74.

## TURNING INWARD

One United States response is to turn mercantilistic and begin protecting its own industrial base. Not only is this not likely to work since it reduces American competitiveness with foreign rivals, but it also goes against the United States philosophy of free-trade and open markets, the very thing that the United States is attempting to gain with Japan.<sup>46</sup> Today's leaders need to learn from history. Between the two world wars, leaders of the United States were plagued by their failure to stimulate trade. Tariffs were raised and the U.S. depression had been transferred to Europe. The rise in protectionism and nationalistic policies caused economic conditions from which world trade never recovered. American officials were not convinced until the end of World War II that, to prevent destructive nationalistic political conflicts, a multilateral world economy, based on strong institutions to regulate trade disparities and bar extreme protectionism, was necessary.<sup>47</sup>

If managed trade practices were adopted by the United States it would focus changes on results rather than allowing market forces to determine outcomes. The desired results would be achieved by mandating the result not the process by which that result is achieved. The free-market philosophy of trade is that as long as the rules for entry and subsequent market activities are fair, the outcome must be fair. Conversely, the managed trade philosophy is that an outcome can be unfair even if the process is fair, because results are affected not only by market access and rules but by past practices, perceptions, or advantages of existing position.<sup>48</sup> The reasons behind

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<sup>46</sup> Moran, p. 81.

<sup>47</sup> Borden, p. 19.

<sup>48</sup> Nanto, p. 14.

the proposal for managed trade with Japan revolve around three explanations. The first is because others perceive Japan's economy and society to be different from other industrialized nations of the world. The second is that the Japanese government has a different relationship in the operations of individual companies than does the United States Government. Although they may not always need governmental guidance, businesses in Japan recognize the government's right to provide it. The view is that the process of negotiations and pressures are damaging the overall relationship with Japan. Bilateral differences must be resolved without resorting to acute pressure and political maneuvering. Although it is being presented as something new, managed trade has already been in practice as voluntary export restraints.<sup>49</sup>

The United States must keep in mind that any action alters the international flow of goods and services. A country's trade policy affects its economic relationship with the rest of the world. Trade policies affect the size of the gains from trade as well as the distribution of gains among trading partners. In disturbing the existing degree of interdependence among nations, trade policy may well have an effect on a trading nation's security.<sup>50</sup>

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<sup>49</sup> Nanto, p. 16.

<sup>50</sup> Leitzel, p. 95.

## CONCLUSION

Increasing tensions between the United States and Japan over the economic imbalance could erode the security relationship as well. This erosion would jeopardize the United States' ability to protect its strategic interests in the Asia-Pacific. United States interests in the region are of foremost importance since the Pacific Ocean is a major maritime highway for navigation and sea lines of communication. Although the majority of Japanese clearly support the continuation of the security alliance, both the alliance and the broader U.S.-Japan relationship are experiencing a number of strains that will likely necessitate modification of the relationship. This support is evident in the fact that even though the Japanese economy has been in recession for more than two years, the Japanese government is constructing replacement airfields on Iwojima and Miyakejima islands for the Naval Air Station in Atsugi.<sup>51</sup> Additionally, Japan is assuming payment for construction of new family housing and labor costs for Japanese employees working on United States Forces Japan bases and they have agreed to shoulder a larger portion of the cost to support United States forces stationed in Japan, approximately a 70 percent burden-share.

The linkage between the economy and national security is becoming ever more evident. Security demands a ready military force. The value of American forward presence in the Asia-Pacific area was highlighted by Admiral Larson, "An active and credible United States forward presence is the cornerstone of future American Asian-Pacific security strategy. Forward presence underscores the vitality of existing United States alliances; it promotes new friendships as host nations observe the benefits of training with United States personnel in an atmosphere of trust and

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<sup>51</sup> Robin Ladd Russell, "Changing Roles of the United States and Japan in the Security of Southeast Asia", (California: Naval Post Graduate School, 1994), p. 112.

confidence; *it encourages and helps underwrite the stable geopolitical climate necessary to promote economic growth* (emphasis added); it assists not only nation building efforts, but the promotion of democracy, by providing working example of the American military's apolitical role; and it increases America's as well as friendly states' military preparedness. Most importantly, forward presence demonstrates on a daily basis the continued United States commitment to remaining an Asian-Pacific power."<sup>52</sup> The need for Japan to bear more of the burden for her defense is necessary to reduce the share absorbed by the United States. The chronic United States trade deficit with Japan has resulted in increasingly vigorous calls in the United States for Japan to change many of its business practices. Such calls are not appreciated by most of the Japanese public, who feel that the trade deficit is a reflection of American faults rather than Japanese unfairness.<sup>53</sup> The friction caused by the economic imbalance between Japan and the United States continues to erode the friendship that has built up between the two countries. United States and Japanese relations must remain strong for the continued prosperity of both nations. Japan and the United States maintain one of the most important economic relationships in the world. The United States alliance with Japan is a pillar of United States security posture for the Asian region. Japan is America's most important ally in the world's most dynamic economic region. It serves as the host nation for key United States military installations and provides billions of dollars each year to support the roughly 47,000 American troops based there.<sup>54</sup> In light of this, one is hard pressed to explain President Clinton's remark, "We do not intend to bear the cost of our military presence in Asia and the burdens of regional leadership only to be shut out of the benefits of growth that stability brings," which he made during the 1993 Asia-Pacific

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<sup>52</sup> Russell, p. 91.

<sup>53</sup> Fukuyama, p. ix.

Economic Cooperation summit meeting in Seattle. Maintenance of regional peace in the Asia-Pacific is contingent on mutual commitments. Though current economic problems exist it is important that the disputes not be overshadowed by the greater need for stability. The United States and Japan must work together to open Japan's markets to assure that both countries will gain their rightful place as global powers, each fulfilling its appropriate role.

In accomplishing this, both countries must be ever conscious of their actions in order to prevent dissolution of the alliance, for: "Trade policy can antagonize governments, generate resentments in populations, . . . influence the tenure of governments, even provoke hostilities."<sup>55</sup>

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<sup>54</sup> Lord, p. 4.

<sup>55</sup> Leitzel, p. 95.

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